



M e m o r a n d u m

To: Panel Members Date: April 24, 2003

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General Counsel

Subject: AMENDMENT TO THE OUT-OF-STATE COMPETITION CRITERIA

This memorandum outlines proposed amendments to Title 22, California Code of Regulations (22 CCR), Section 4416, which sets out the Employment Training Panel's (ETP) out-of-state competition requirements for standard retraining projects. The revisions address the Fiscal Year 2002-03 Strategic Plan objective to continuously review training-related regulations and policies, including refining the criteria for out-of-state competition.

Background

Unemployment Insurance Code Section 10200(a)(1) states, in part, that the Panel shall "foster retention of high-wage, high-skilled jobs in manufacturing and other industries that are threatened by out-of-state competition." In 1996, the Panel promulgated 22 CCR Section 4416 to further define out-of-state competition and outline specific requirements for standard retraining projects developed for the Panel's consideration. This regulation has served as the basis for determining whether an entity is eligible for ETP funds. Since 1996, the Panel has not substantially revised the basic criteria for out-of-state competition.

The proposed amendments, as outlined in Attachment 1, focus on five major areas: (1) implementation of the North American Industrial Classification System; (2) expansion of industries deemed to face out-of-state competition; (3) clarification of service industry criteria; (4) clarification of the corporate headquarters provisions; and (5) clarification of call center requirements.

1. North American Industrial Classification System

The North American Industrial Classification System (NAICS) was developed to standardize the collection and analysis of North American economies by governmental agencies in Canada, Mexico and the United States. NAICS establishes 20 different industry sectors based on their primary activities.

Sections 4416(b) and 4416(c) have been updated based upon the NAICS. Since this revision substitutes currently existing Standard Industrial Classification (SIC) categories with their NAICS counterparts, there will be no adverse impact to the entities currently eligible for ETP-funding under the NAICS subsections.

2. Expansion of Industries Deemed to Face Out-of-state Competition (Section 4416(c))

The industries deemed by the Panel to face out-of-state competition under Section 4416(c) should be expanded to include the following industries: (a) Scientific Research, Testing Laboratories and Engineering, (b) Entertainment Postproduction and Teleproduction, and (c) Software Design and Engineering. NAICS provides more detailed classifications than the previous SIC system. This change enables the Panel to more effectively identify and target these industries that historically have high-wage, high-skilled jobs and face out-of-state competition.

3. Service Industries, Section 4416(a)(3),(4)

At the November 2002, Panel Meeting, the Panel requested staff strengthen the criteria used to determine eligibility for employers that provide services to customers located inside and outside of California. Sections 4416(a)(3), (4) currently define eligible companies as those that provide services to customers located outside of California or in-state in direct competition with providers of the same services located outside of California.

Although Section 4416(a)(3) does not specify what percentage of revenues must originate from out-of-state, ETP practice has required that out-of-state sales revenues must be at least 20 percent of a company's gross revenues. Upon review, staff determined that this subsection's criteria could be strengthened by increasing the percentage requirement to 25 percent of gross annual revenues. Staff has determined that this increase would not significantly lower the training population determined eligible under this subsection.

Regarding Section 4416(a)(4), the Panel has noted that, without specific criteria, some companies have encountered problems demonstrating that their provision of in-state services face a significant threat from providers of the same services located outside the state. To clarify this section, staff has revised the regulation to require that the applicant service provider compete with businesses, which, on an ongoing basis, provide the same service in California solely from locations outside the state.

4. Corporate Headquarters and Support, Section 4416(d)(1)

Currently, Section 4416(d)(1) specifies that a company facility will be deemed to face out-of-state competition if it is either the California corporate headquarters of a company which does significant business outside the state or if the facility provides significant support to a company's offices located outside of California. Through this subsection, the Panel acknowledges that the corporate headquarters of a company which does a significant amount of business outside California could readily move its headquarters or support facility to a location outside of California with minimal impact to its operations. However, this subsection does not currently specify what constitutes such a significant out-of-state presence.

To clarify this section, staff has developed three criteria under which a company can establish that it maintains a significant presence outside of California. It is not anticipated that incorporating the clarifying criteria will significantly diminish the numbers of eligible project applicants.

5. Call Centers

The eligibility requirements for call centers under the out-of-state competition regulation must be clarified. A review of contracts approved from July 1, 2000, through March 30, 2003, indicates ETP has increasingly funded call centers in recent years. Over this period, the Panel approved 41 contracts that involved some training for call centers.

Funding for call centers increased by 20.2 percent from FY 00/01 to FY 01/ 02; and, if the current rate of such funding continues in FY 02/03, \$16.4 million could potentially be approved for call centers this fiscal year, thereby increasing call center funding by 33.3 percent over last year.

Another issue is whether some California call centers are actually competing directly with out-of-state call centers. In the telecommunication industry alone, some ETP contractors have identified their out-of-state competitors as call centers belonging to other ETP-funded contractors.

To address these issues, staff has created a definition of call center that will target only those call centers that do not provide telemarketing services and have over 50 percent of their call volume originating from outside of California.

Recommendation

That the Panel approve the proposed revisions, as provided in Attachment 1, and direct staff to initiate the regulatory process to amend 22 CCR Section 4416, which will result in:

- 1) Implementation of the North American Industrial Classification System;
- 2) Addition of (a) Scientific Research, Testing Laboratories and Engineering, (b) Entertainment Postproduction and Teleproduction, and (c) Software Design and Engineering as industries deemed to be facing out-of-state competition;
- 3) Clarification of service industry requirements;
- 4) Clarification of the corporate headquarters provisions; and
- 5) Clarification of call center requirements.

4416. Out-of-State Competition.

Attachment 1

- (a) For purposes of Panel funding, out-of-state competition exists if ~~the individual function and/or unit of a company's individual facility, functional group or unit~~ for which training funds are sought meets the following conditions:
- (1) produces a product sold out-of-state; and/or
 - (2) produces a product sold in-state which competes with products produced out-of-state; and/or
 - (3) provides a service directly to or on behalf of customers located out-of-state; and/or revenues derived directly from this service exceed 25% of the gross annual revenues for that individual facility, functional group or unit; and/or
 - (4) provides a service in the state in competition with businesses, which, on a continuing basis, providers of provide the same service in this state solely from locations located outside the state.
- (b) A company engaged in manufacturing is deemed to meet the out-of-state competition requirement for purposes of Panel funding if that company meets the definition of ~~Division D Sector 31-33, Manufacturing as contained in the Standard Industrial Classification (SIC) North American Industrial Classification System (NAICS) Manual, or is assigned by the Employment Development Department a SIC NAICS within Division D, Manufacturing, Subsectors 311-339 Major Groups 20-39~~ as follows:

**STANDARD INDUSTRIAL CLASSIFICATIONS NORTH AMERICAN INDUSTRIAL
CLASSIFICATION SYSTEM OF
THE MANUFACTURING INDUSTRY**

Division D.: Manufacturing	
Major Group Number <u>Subsector</u>	Products
20 <u>311</u>	Food and Kindred products
24 <u>312</u>	<u>Beverage and Tobacco</u> products
<u>313</u>	<u>Textiles</u>
22 <u>314</u>	Textile Mill Products, <u>Except Apparel</u>
23 <u>315</u>	Apparel Products and other finished products made from fabrics and similar materials

Division D.: Manufacturing	
Major Group Number Subsector	Products
31 <u>316</u>	Leather and Allied leather Products
24 <u>321</u>	Lumber and Wood Products, Except Furniture
26 <u>322</u>	Paper <u>Manufacturing</u> and allied products
27 <u>323</u>	Printing <u>And Related Manufacturing</u> , publishing and allied industries
29 <u>324</u>	<u>Coal</u> , Petroleum Refining and Related Industries
28 <u>325</u>	Chemicals and <u>Refined</u> allied Products
30 <u>326</u>	<u>Plastics and</u> Rubber and miscellaneous plastic products
32 <u>327</u>	<u>Nonmetallic Mineral</u> Stone, clay, glass and concrete products
33 <u>331</u>	Primary Metal <u>products</u> industries
34 <u>332</u>	Fabricated Metal Products, except machinery and transportation equipment
35 <u>333</u>	Industrial and commercial machinery and computer equipment
<u>334</u>	<u>Computer and Electronics Equipment</u>
36 <u>335</u>	Electronic and other electric Equipment, <u>Appliances and Related Components</u> , except computer equipment
37 <u>336</u>	Transportation Equipment
25 <u>337</u>	Furniture and <u>Related Products</u> Fixtures
39 <u>339</u>	Miscellaneous Manufacturing Industries
38	Measuring, analyzing and controlling instrument; photographic, medical and optical goods; watches and clocks

- (c) companies assigned by the Employment Development Department to any of a NAICS Code within the following Sectors, Subsectors, Industry Groups and/or Industries SIC codes are also deemed to meet out-of-state competition:

<u>Major Group Subsector</u>	Industry Group(s) Title or Number	Products
01 <u>111</u>	Agricultural <u>Crop Production</u>	Crops
02 <u>112</u>	Agricultural <u>Animal Production</u>	Livestock and Animal Specialties
08 <u>113</u>	<u>Logging and Forestry</u> Industry Group 081 Industry Group 083	<u>Timber Tracts and Nursery Products</u> Forest Nurseries
09 <u>114</u>	Fishing, Hunting & Trapping	<u>Marine and Wildlife Products</u>
13 <u>211</u>	Industry Groups <u>2111</u> 131 & 132	Oil & Gas Extraction
12 <u>212</u>	Industry Groups <u>2121</u> 122 & 123	Coal Mining
40 <u>212</u>	Industry Groups <u>2122</u> 401-406, 409	Metal Mining
44 <u>212</u>	Industry Groups <u>2123</u> 441-447 & 449	Mining of Nonmetallic Minerals
73 <u>511</u>	<u>Publishing Industries</u> Industry Number 7372	<u>Newspapers, Books and Prepackaged Software</u>
78 <u>512</u>	Industry <u>51211, 51219</u> 7842	<u>Motion Picture and Video Production, Tele-production and Postproduction</u>
<u>541</u>	<u>Industries 54138, 54138, 54171</u>	<u>Engineering Services, Testing Laboratories and Scientific Research</u>
<u>541</u>	<u>Industries 541511, 541512</u>	<u>Custom Computer Programming and Computer System Design</u>

(d) A company's facility, functional group and/or unit is also deemed to be facing out-of-state competition if it meets any of the following categories:

(1) The facility applicant is located in California, and is the Corporate Headquarters of a company that does maintains a significant presence business outside of California.

(A) The company will be deemed by the Panel to be maintaining a significant presence outside of California if it meets at least one of the following criteria:

(1) more than 25% of total gross annual revenues are derived from permanent company facilities, offices, operations, divisions, branches, stores, or franchises located outside of California; and/or

(2) 25% or more of the permanent company facilities are located outside of California; and/or

(3) 25% or more of the permanent full-time employees are employed at company facilities located outside of California.

(B) In addition to the Corporate Headquarters facility, a functional group and/or unit company's facility is eligible if it provides significant support services to the company's facilities, offices, operations, divisions, branches, stores, or franchises as part of the company's significant presence located outside of California.

(2) The applicant is a mortgage bank or related institution engaged in the packaging/sales and/or servicing activities related to loans. These loan activities must be conducted by the bank or institution within California. Only those jobs directly involved with the mortgage banking function will be considered for training.

(3) The applicant is a destination resort, convention/conference center or convention/conference hotel that competes nationally and/or internationally for customers, as set forth below:

(A) Destination resort means an establishment and its affiliated facilities which:

1. is a recognized destination, or
2. operate in conjunction with, or by virtue of, a destination recreational complex or attraction, and have derived at least 25 percent of its gross annual revenue from out-of-state visitors.

(B) For purposes of this subsection, the term "destination" refers to the establishment, recreational complex, or attraction being itself the primary reason for people traveling to it. A city is not, in and of itself, a destination.

- (C) For purposes of this subsection, the term "convention/conference center" means an establishment primarily dedicated to holding conventions, conferences, and/or trade shows or exhibits.
 - (D) For purposes of this subsection, the term "convention/conference hotel" means an establishment that derives at least 25 percent of its gross annual revenue (inclusive of rooms and food/beverage revenues) from conventions, conferences, and/or trade shows or exhibits involving transient lodging requirements.
 - (E) A destination resort, convention/conference center or convention/conference hotel will be deemed to compete nationally and/or internationally for customers if it meets at least three of the following criteria:
 - 1. Participates in out-of-state sales missions or trade shows;
 - 2. Routinely conducts out-of-state sales efforts;
 - 3. Routinely advertises in media in which its out-of-state competitors also advertise;
 - 4. Contributes financially to joint community based out-of-state marketing efforts;
 - 5. Maintains a marketing plan which addresses the national/international market; or
 - 6. Documents that it is in competition with similar establishments outside of California.
- (4) The facility is a call center with over 50% of its annual call volume originating from outside of California. For purposes of Panel funding, a call center is defined as a facility which meets both of the following criteria: (a) is primarily engaged in taking orders or providing customer service using the telephone or internet on behalf of company customers; and (b) does not provide any telemarketing services. If the company facility is not primarily engaged in the call center function, only the functional groups and their immediate functional support will be considered under this subsection.

Authority: Section 10205(l), Unemployment Insurance Code.
Reference: Section 10200(a), Unemployment Insurance Code.
Effective: July 19, 1996